Canyons School District, Utah

New Issue Report

Ratings

Issuer Default Rating (IDR)	AAA

New Issue

General Obligation Bonds (Utah School Bond Guaranty Program), Series 2018B	AAA

Outstanding Debt

General Obligation Bonds[a]	AAA

[a]The 'AAA' rating is based on a guarantee provided by the Utah School Bond Default Avoidance Program, which is rated 'AAA'/Stable by Fitch. Canyons School District's GO bonds have a 'AAA' underlying rating from Fitch, reflecting the district's credit quality without consideration of the guarantee provided by the Utah School Bond Default Avoidance Program.

Rating Outlook

Stable

Analysts

Alan Gibson
+1 415 732-7577
alan.gibson@fitchratings.com

Andrew Ward
+1 415 732-5617
andrew.ward@fitchratings.com

New Issue Summary

Sale Date: Competitive sale on Oct. 23, 2018.

Series: $75,000,000 General Obligation (GO) Bonds (Utah School Bond Guaranty Program), Series 2018B

Purpose: To fund school capital improvement projects.

Security: The bonds are general obligations of the district, payable from the proceeds of unlimited ad valorem property taxes levied on all taxable property within the district.

Analytical Conclusion

The 'AAA' IDR and underlying rating on the outstanding GO bonds reflect the Canyon School District’s (the district) solid financial operations, flexible labor environment, and low debt and pension burden. The district's superior inherent budget flexibility has resulted in exceptionally strong gap-closing capacity. The GO bonds are supported by a growing tax base.

Key Rating Drivers

Revenue Framework: 'aaa'
Strong general fund revenue growth will likely continue in line with, or above, national economic performance. The district's independent legal ability to raise revenues is high, which is unusual for a U.S. school district.

Expenditure Framework: 'aa'
Spending growth will likely remain in line with, to marginally above, anticipated revenue growth. The district enjoys solid expenditure and labor flexibility.

Long-Term Liability Burden: 'aaa'
The district's combined debt and unfunded pension liability is low relative to its resource base. Fitch Ratings expects this burden to remain low and the direct debt amortization rate to remain slightly below average, after the issuance of additional debt in the short- to medium-term. Pension system contributions have stabilized, and liability related to the closed other post-employment benefit (OPEB) plan is winding down.

Operating Performance: 'aaa'
The district has exceptionally strong gap-closing capacity, which should ensure financial resilience during economic downturns.

Rating Sensitivities

Solid Financial Operations: Fitch expects that the district will continue to exercise sound budget management. Continued sufficient reserve levels through the economic cycle would enable the district to maintain a 'AAA' IDR.

Rating History - IDR and GO Bonds

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	10/1/18
AAA	Upgraded	Stable	2/13/13
AA+	Assigned	Positive	3/15/11

Credit Profile

Canyons School District covers about 192 square miles of southeastern Salt Lake County. It has approximately 34,000 students attending 47 schools and an adult and community education program, making it the fifth largest school district in Utah. The district's taxable assessed valuation (TAV) rebounded strongly after a 7% recessionary decline. Between fiscal years 2014 and 2019, TAV grew by 48%, with further strong growth projected because of ongoing residential and commercial construction.

The district is primarily residential with an established commercial base and it benefits from being an integral part of the Salt Lake City metro economy. Nevertheless, wealth characteristics vary markedly among the district's component communities, which include the cities of Midvale (IDR 'AA'/Stable), Cottonwood Heights, Sandy, and Draper. The district includes some of the wealthiest communities in the state, while other areas are more challenged, with significant portions of their students eligible for free and reduced lunch programs.

Revenue Framework

The district's funding comes from a combination of property taxes imposed by the school board, state-imposed personal income and corporate franchise taxes, and federal sources. In fiscal 2017, local revenues accounted for almost 40% of general fund revenues, and state sources, almost 54%, with the balance coming from federal sources. The weighted pupil unit (WPU) is the statutory allocation methodology for equalized school funding across the state. It increased between 2% to 4% in each of fiscal years 2016 to 2019. In fiscal 2019, the state is also providing another 1.5% WPU increase in flexible allocation.

Fitch expects that strong general fund revenue growth will likely continue in line with, or above, national economic performance. The district has experienced strong revenue growth since its inception. Assuming a proportionate share of pre-fiscal 2010 Jordan School District revenues, its 10-year revenue growth has exceeded national GDP growth. This has been the result of slowly increasing student enrollment and improved state funding. The district expects student enrollment to be stable and is not experiencing any new charter school competition.

The district has a high independent legal ability to raise revenues. It could raise over $26 million more per year (approximately 10% of budgeted fiscal 2019 general fund revenues), subject to the advisory truth-in-taxation public hearing process, under the board local tax levy set by the district's school board. Such an increase would not result in a reduction of state funding. After completing its building plan in the next seven years or so, the district could also reduce its capital outlay levy and commensurately increase its operations and maintenance levy to direct an additional $2 million to $3 million in tax revenues to the general fund.

The district has not increased the property tax rate since its inception. However, it might need to do so sometime during fiscal years 2020 through 2022 to absorb rising personnel costs in a competitive job market.

Expenditure Framework

The majority of spending is on instruction costs (61% of fiscal 2017 general fund spending), with a further 10% spent on facilities operating costs. The district's fiscal 2018 general fund budget absorbed approximately $18 million in increased employee remuneration and benefit costs (approximately 7% of budgeted spending), largely spurred by Utah's very competitive teacher market. Further remuneration pressure has resulted in the fiscal 2019 budget,

Related Research

Fitch Rates Canyons School District, UT's GOs 'AAA'; Outlook Stable (October 2018)

Canyons School District, Utah (December 2017)

Related Criteria

U.S. Public Finance Tax-Supported Rating Criteria (April 2018) absorbing over $7 million in additional teacher salary and benefit costs (less than 3% of budgeted spending, conservatively assuming no attrition, which customarily saves up to $2 million annually).

Based on the district's patterns of revenue and spending, Fitch expects future general fund expenditures to be in line with, to marginally above, general fund revenue growth. The district's carrying costs related to debt repayment and pension contributions are moderate relative to the district's resource base, leaving it with solid expenditure flexibility.

The district considers personnel costs its area of greatest spending flexibility. The district only enters into annual teacher contracts based on each year's available budget. If the district needed to reduce expenditures, it would likely utilize the flexibility of its annual teacher contracts to modify future step and column increases and cost of living adjustments. The district could also increase class sizes, eliminate support positions, and move more support employees to hourly positions without benefits.

Long-Term Liability Burden

The district's overall debt and pension burden is low, at 5% of personal income. The majority of the debt burden is direct district debt, which includes a 58% portion of GO debt issued by Jordan School District prior to the division of the two districts in fiscal 2010 and subsequently refunded in 2014.

Although the stable student enrollment projections means the district does not face pressure to construct new schools, it has identified $300 million in needed facility upgrades and modernization. In November 2017, district voters approved up to $283 million in GO bonds (with 58% support). District officials expect to issue this debt in five tranches through fiscal 2022, starting with the district's 2018 and 2018B GO bonds. The district aims to keep its property tax rate as close to the current level as possible. Based on a pro forma schedule for three future tranches of GO bonds, Fitch does not expect the district's direct debt burden to increase materially with the issuance of new debt. Amortization looks likely to be slightly below average, at 45%, in 10 years.

Once the district's building program is complete, which management expects by fiscal 2025 at the latest, the district expects to use a mixture of pay-as-you-go and GO bond funding for future capital improvement projects. It expects that any future bond measure in eight to 12 years' time would be for a smaller $100 million to $150 million par amount.

The district participates in the state retirement pension system and makes its annual actuarially-determined contributions. Using Fitch's 6% discount rate, which is more conservative than the state retirement pension system's 7.2% rate, the district's pension liabilities are approximately 74% funded in fiscal 2017. The district's employer contributions have now stabilized after some years of increases to offset recessionary investment losses. The closed OPEB plan's remaining liability is declining as the program winds down.

Operating Performance

The district has exceptionally strong gap-closing capacity. For details, see Scenario Analysis, page 5.

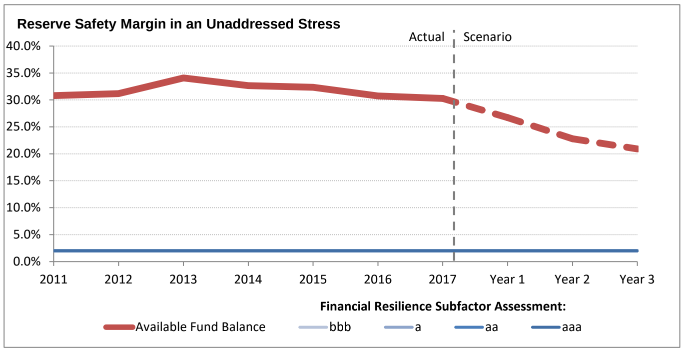
The district ended its eighth year of operations with a strong unrestricted general fund balance and ample liquidity and borrowable resources. The district increased its unrestricted general fund balance to over $73 million (30% of spending) in fiscal 2017, from almost $36 million (19% of spending) at its inception in fiscal 2010. Within its general fund balance, the district continues to roll forward its economic stabilization reserve at the maximum amount allowed by state statute: 5% of fiscal 2018 general fund budgeted expenditures, or more than $13 million. Additionally, the district continues to include 105% of its accrued actuarial OPEB liability within the committed general fund balance.

The district projects that the fiscal 2018 general fund balance will decline very slightly, by approximately $52,000, due to one-time expenditures. The budgeted deficits in fiscal years 2019 and 2020 are largely due to state budgetary requirements. The district has to budget use of the entire unassigned general fund balance (over $22 million at fiscal 2017 year-end). Typically, the district significantly outperforms its conservative budgets and its general fund balances are expected to remain very strong through fiscal 2022.

In addition to strong general fund liquidity, in an emergency, the district could also borrow from its internal service fund (nearly $4 million) and its capital outlay fund. The capital outlay fund balance is budgeted to be almost $33 million by the end of fiscal 2019 but lower in future years as funds are expended on the district's capital improvement program. Current projections show the capital outlay fund balance will decrease to $10 million when all the district's capital improvement projects have been completed.

Canyons School District (UT)

Scenario Analysis



Analyst Interpretation of Scenario Results:

The district has exceptionally strong gap-closing capacity. The district's unrestricted general fund balance has always been well in excess of Fitch's 'aaa' reserve safety margin. Given low revenue volatility and superior inherent budget flexibility, Fitch expects the district to maintain a 'aaa' reserve safety margin during any periods of economic stress.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(1.0%)	1.6%	4.1%
Inherent Budget Flexibility	Superior		

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2011	2012	2013	2014	2015	2016	2017	Year 1	Year 2	Year 3
Total Revenues	207,625	209,878	218,085	220,336	223,091	239,653	242,501	240,076	243,802	253,705
% Change in Revenues	-	1.1%	3.9%	1.0%	1.3%	7.4%	1.2%	(1.0%)	1.6%	4.1%
Total Expenditures	197,191	204,391	212,582	219,910	222,461	239,438	242,407	247,256	252,201	257,245
% Change in Expenditures	-	3.7%	4.0%	3.4%	1.2%	7.6%	1.2%	2.0%	2.0%	2.0%
Transfers In and Other Sources	-	-	-	-	-	-	-	-	-	-
Transfers Out and Other Uses	170	255	306	478	387	178	153	156	159	162
Net Transfers	(170)	(255)	(306)	(478)	(387)	(178)	(153)	(156)	(159)	(162)
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	10,264	5,232	5,197	(52)	243	37	(59)	(7,336)	(8,558)	(3,702)
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	5.2%	2.6%	2.4%	(0.0%)	0.1%	0.0%	(0.0%)	(3.0%)	(3.4%)	(1.4%)
Unrestricted/Unreserved Fund Balance (General Fund)	60,804	63,813	72,516	71,956	72,109	73,625	73,410	66,074	57,516	53,815
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	60,804	63,813	72,516	71,956	72,109	73,625	73,410	66,074	57,516	53,815
Combined Available Fund Bal. (% of Expend. and Transfers Out)	30.8%	31.2%	34.1%	32.6%	32.4%	30.7%	30.3%	26.7%	22.8%	20.9%

Reserve Safety Margins	Inherent Budget Flexibility				
	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	16.0%	8.0%	5.0%	3.0%	2.0%
Reserve Safety Margin (aa)	12.0%	6.0%	4.0%	2.5%	2.0%
Reserve Safety Margin (a)	8.0%	4.0%	2.5%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.0%	2.0%	2.0%	2.0%	2.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

The ratings above were solicited and assigned or maintained at the request of the rated entity/Issuer or a related third party. Any exceptions follow below.